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Summary of the economic and social situation in Africa, 2001

Recent economic trends in Africa and prospects for 2002

Summary

Africa grew faster than any other developing region in 2001, reflecting better macroeconomic management, strong agricultural production, higher than expected exports under the United States of America's African Growth and Opportunity Act, currency depreciation in the largest economy — South Africa — and the cessation of conflicts in several countries. These gains were made amid the turbulence created by the global economic slowdown and the attacks of 11 September on the United States. But Africa's average gross domestic product growth of 4.3 per cent in 2001 masks wide disparities, with growth ranging from 65 per cent in Equatorial Guinea to -7 per cent in Zimbabwe. Moreover, economic growth remains fragile, and at current rates Africa will not achieve any of the millennium development goals set by the United Nations. Still, there are many reasons for cautious optimism about Africa's medium-term prospects — including the opportunities created by the United States African Growth and Opportunity Act, the European Union's "Everything but Arms" initiative, the New Partnership for Africa's Development, and the launching of the Doha development round and the Africa Union. Ultimately, though, Africa's future depends on how it addresses economic and political governance, resolves civil conflicts and responds to the need for deeper economic and social reforms.

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Africa was the only developing region with faster growth in 2001

1. Forecasts made soon after the terrorist attacks on 11 September 2001 in New York and Washington, D.C., predicted that economic growth would stagnate in Africa because of lower commodity prices, reduced foreign direct investment and diminished private capital flows. But the global slowdown has had a much less pronounced impact on Africa than expected. Output has remained relatively strong, with growth accelerating in 2001 in countries such as Ethiopia (8.7 per cent growth), Mozambique (9.2 per cent), and Uganda (5.4 per cent). Africa's overall gross domestic product (GDP) is estimated to have increased from 3.5 per cent in 2000 to 4.3 per cent in 2001.

2. Africa's resilience against the global slowdown reflects many factors:

- Lower oil prices, which helped 42 oil-importing African countries by easing pressures on foreign exchange, inflation and public spending;
- Continued improvements in agricultural output across the region — particularly in Morocco, Tunisia and East Africa;
- Sounder economic management, resulting in stronger economic fundamentals in many countries — with lower inflation, better fiscal positions and stronger external positions;
- Higher than expected exports under the United States African Growth and Opportunity Act;
- Reduced conflict and insecurity in Burundi, the Democratic Republic of the Congo, Eritrea, Ethiopia, Guinea and Sierra Leone;
- Currency devaluations in the largest economy — South Africa — and rising domestic demand across the continent, buoyed by strong remittances.

3. The significance of these factors should not be overstated, however. Many African countries are dependent on international markets, and a sharp and sustained deterioration in global conditions will eventually take a toll on the region's economies.

Changing commodity prices provide mixed blessings for Africa

4. Commodity prices are the main channel by which external weaknesses are transferred to most African economies. Global non-oil commodity prices recovered by 2 per cent in 2000 after dropping sharply in 1998 and part of 1999, but prices remained below 1996-1997 levels. Moreover, the World Bank's price index for primary commodities from low- and middle-income countries has fallen steadily since 1995.

5. Terms of trade show no signs of improving in 2001-2002. In the first 11 months of 2001 the prices of primary commodities fell in response to the strong downturn in global economic activity. Lowered growth expectations for the world economy after 11 September accentuated weak demand, while supply remained high and the dollar (the currency in which most commodities are priced) was strong. In September 2001 average commodity prices were 17 per cent below their cyclical peak of one year earlier.

6. Commodity price movements provided mixed blessings for Africa. For most African countries, where oil accounts for up to 30 per cent of merchandise imports, the 56 per cent increase in oil prices in 1999-2000 was a major cause of the inflation and economic slowdown in 2000. Thus, the drop in oil prices in 2001 freed resources for other imports and minimized inflationary and other pressures. In Egypt, for example, lower oil prices eased pressures on interest rates, exchange rates and domestic investment. Moreover, oil exporters were able to sustain growth in 2001 using the substantial revenue from the 1999-2000 boom. Thus, lower oil prices generally had a positive effect on Africa, where net energy exports constitute only 5 per cent of GDP.

7. Many African countries, however, depend on commodity exports — and the outlook for commodities is not good. A recovery in commodity prices will require more than a modest recovery in global demand. To draw down inventories, global growth of 4 to 5 per cent is needed.

Tourism and remittances experienced steady growth

8. Prospects for tourism in sub-Saharan Africa remain strong despite the attacks of 11 September. Tourism accounts for more than 11 per cent of the region's GDP and is expected to grow by more than 5 per cent a year in real terms through 2010. With sub-Saharan Africa's tropical weather, exotic wildlife, pristine coastal areas, proximity to Europe and low wages, tourism has enormous growth potential.

9. Kenya's recent efforts to address problems in the tourism industry seem to have paid off. International arrivals increased by 10 per cent between the first eight months of 2000 and the same period in 2001, from 309,000 to about 340,000.

10. Kenya and other African destinations stand to benefit from the steep fall in United States and European air traffic since 11 September. For example, South Africa — another major destination for African tourism — has seen an increase in international flights as foreign airlines redraw routes that had gone through the United States. South Africa is doing well because it is considered a relatively safe destination.

11. Western Union — the United States financial services giant, with 20,000 outlets in 45 African countries — recently reported that remittances to Africa from Europe, the Middle East and the United States remained strong through the fourth quarter of 2001. Remittances from Africans working abroad have powerful multiplier effects, with each dollar generating additional dollars for businesses that supply products bought with these resources. Remittances also support consumer demand during economic crises.

12. Over the past decade worker remittances to Africa have grown significantly. According to the International Monetary Fund (IMF), remittances exceeded $100 billion in 1999, but actual remittances are likely much higher. For example, Western Union estimates that $100 million in remittances is transferred across southern African borders each year through an informal system of taxi and bus drivers.

African exports to the United States jumped

13. The value of United States imports from Africa has grown considerably in recent years, from about $1.5 billion a month in 1999 to $2.3 billion a month in 2000. African exports received a further boost with the January 2001 implementation of the United States African Growth and Opportunity Act (see box 1). Although total United States imports fell between January and June 2001, imports covered by the African Growth and Opportunity Act increased sharply — suggesting that these African exports may be insulated from the United States economic slowdown.

14. The composition of these exports explains this pattern. Between January, and September 2001 about 91 per cent were energy-related products, reflecting the diversification of sources for such imports to the United States. Textiles and apparel, transportation equipment (vehicles), minerals and metals, and agricultural products accounted for the rest. The main exporters under the African Growth and Opportunity Act were Nigeria (accounting for 56 per cent of the total), South Africa (22 per cent), and Gabon (12 per cent). Among the 10 top exporters, South Africa provided the most varied mix of products, with transportation equipment accounting for 57 per cent, followed by minerals and metals (24 per cent), agricultural products (13 per cent), and textiles and apparel (6 per cent).

Box 1
The African Growth and Opportunity Act — a boost for exports, employment and investment

In June 2000 the United States Congress passed the African Growth and Opportunity Act. Among other benefits, the act eliminated United States duties on textile imports from eligible sub-Saharan countries — good news not just for those countries but also for the international textile industry, which is always seeking new low-wage countries with good access to industrial country markets.

The preferential tariffs provided by the act have provided an enormous boost to the textile industry in Madagascar, one of the first countries to qualify for benefits. Textile exports surged in 2001, and in the first half of the year United States imports from Madagascar totalled $133 million — a 115 per cent jump from the first half of 2000. Among the most visible beneficiaries of the textile boom are women who previously earned low, unpredictable incomes selling produce or working in rice fields. Moreover, the boom has spread to other industries such as construction and engineering. Formal employment has more than doubled, boosting tax revenue.

In addition, foreign investment has risen sharply in Madagascar and the 12 other sub-Saharan countries that have qualified for trade benefits under the United States legislation. Lesotho has plans for more than $120 million in new investments. In Kenya the act will create 50,000 jobs directly and another 150,000 indirectly.

To ensure long-term benefits from better access to United States markets, African countries must diversify their economies, investing in the infrastructure and education that attract higher-tech companies. Indonesia and Malaysia achieved this economic transformation in the 1970s, and Mauritius did so recently.

Source: Economic Commission for Africa.

Africa's emerging markets experienced a sharp increase in private capital flows

15. Unlike emerging markets in other regions, those in Africa — Algeria, Egypt, Morocco, South Africa and Tunisia — were not hurt by the attacks of 11 September. In fact, between 2000 and 2001 net private flows to these countries nearly doubled, from $4.9 billion to $9.5 billion. In addition, net equity investment jumped from $5.2 billion to $9.3 billion, mainly reflecting large-scale deals in Morocco and South Africa. Net direct equity grew from $3.5 billion to $4.8 billion, driven by privatizations in Algeria and Morocco, and despite weaknesses in global equity markets, net portfolio equity flows shot from $1.7 billion to $4.5 billion, Net outflows are likely in 2002, however, as risk-averse investors avoid emerging equity markets. Elsewhere in Africa, stock markets had mixed performances in 2001.

16. Private credit flows to Africa's emerging markets increased slightly, from a net outflow of $400 million in 2000 to an inflow of $200 million in 2001. Still, this is an extremely modest amount for a group that includes Africa's largest economy — South Africa — relative to other regions and to Africa's needs.

17. Bond market and other net lending by non-banks was flat in 2001, reflecting fewer primary bond issues and significant net repayments. Net non-bank lending is expected to grow marginally in 2002, to $500 million. Immediately after the attacks of 11 September the spread between United States Treasury bonds and JPMorgan's emerging market index widened by 81 basis points (0.81 per cent). But some African countries were hit even harder — for example, spreads on Nigerian debt had fallen to nearly 1,400 basis points in May 2001 but rose to more than 2,000 basis points in mid-September.

18. Emerging market equity prices fell particularly hard after the attacks of 11 September. By 18 September emerging market equity prices, as measured by the Morgan Stanley Capital International index, were 23 per cent lower than at the beginning of the year. But prices had started to fall significantly in July, reflecting increased pessimism and uncertainty about the global economic slowdown. Except for South Africa's exchange, which rose 26 per cent, Africa's emerging equity markets lost value in 2001.

Africa has seen a shift in foreign direct investment

19. Foreign direct investment is the most important source of external finance for developing countries — more important than commercial loans, portfolio investment and official development assistance. Africa's share of foreign direct investment in

developing countries dropped from 25 per cent in the early 1970s to just 5 per cent in 2000, but this average figure masks a number of interesting trends. First, new sources of foreign direct investment have emerged. In the past most foreign direct investment in Africa came from a handful of Organisation for Economic Cooperation and Development (OECD) countries — mainly France, the United Kingdom and the United States. During the 1990s, however, foreign direct investment from Canada, Italy, the Netherlands, Norway, Portugal and Spain increased from less than 10 per cent of the total to nearly 25 per cent. Furthermore, foreign direct investment from developing Asian economies has also increased, led by the Republic of Korea and followed by China, India, Malaysia and Taiwan Province of China. Finally, during the 1990s intra-African foreign direct investment rose, notably by firms from South Africa and Mauritius.

South Africa leads intra-African flows

20. South Africa is by far the continent's most important source of foreign direct investment. Since 1994 South African foreign direct investment in other African countries has averaged $1 billion a year. South Africa is home to three of the world's largest transnational corporations: Sappi Limited (with $4.6 billion in foreign assets in 2000), Barlow Limited ($1.8 billion) and South African Breweries ($700 million). South African Breweries, the world's fourth largest brewer (by volume), operates in 11 African countries and has extensive holdings in India and Central and Eastern Europe. Similarly, Nedbank, the South African banking giant, has subsidiaries or associated companies in Lesotho, Malawi, Mauritius, Mozambique, Namibia, Swaziland and Zimbabwe. It also owns 40 per cent of HSBC Equator Bank, which is based in London but has offices in Angola, Côte d'Ivoire, Ghana, Kenya, Mozambique, South Africa, Uganda and Zambia. Mauritius is emerging as an important investor in Côte d'Ivoire, Madagascar, Mozambique, Seychelles and South Africa. Ghana's Ashanti Goldfields — the country's largest company, employer and foreign exchange earner — has operations valued at $2 billion in Guinea, Tanzania and Zimbabwe. It was also the first sub-Saharan company to be listed on the New York Stock Exchange.

Uganda attracts flows in its nascent manufacturing sector

21. From 1988 to 1993 foreign direct investment in Uganda averaged just $9 million a year. But in 1994 foreign direct investment jumped to $88 million, and since 1995 it has been more than $100 million a year. Though small, Uganda's manufacturing activities have attracted the most foreign direct investment — particularly beverages, but also textiles, sugar, cement, footwear, packaging, plastics and food processing. Most foreign direct investment in agriculture, forestry and fishing has gone to coffee, tea and cotton plantations. The liberalization of telecommunications resulted in a major investment by MTN, a South African company that was awarded Uganda's second service licence. In addition, the United States-owned AES Power Nile is starting a major power project at Bujagali Falls.

Aid to Africa remains low and volatile

22. Aid to Africa increased from just less than $1 billion in 1960 to $32 billion in 1991. But by the end of the 1990s, aid had fallen to almost half the 1991 level.

(Here aid is defined as gross official development assistance — whether grants or concessional loans — from multilateral and bilateral sources.)

23. The countries that make up the Development Assistance Committee (DAC) of OECD are the largest source of African aid, though their share of the total fell from 72 per cent in 1970 to 63 per cent in 1999. Multilateral organizations are the second largest source, and their share of the total jumped from 21 per cent in 1970 to 35 per cent in 1999. Africa's remaining aid comes from Arab countries, which accounted for 7 per cent of the total in 1970 and 2 per cent in 1999.

24. Aid from DAC countries is extremely volatile, rising from $3.1 billion in 1970 to $23.4 billion in 1991 — then falling to $11.8 billion in 1999. Aid from multilateral organizations is less volatile, increasing from $0.4 billion in 1970 to $9.5 billion in 1994 and then falling to $6.6 billion in 1999. Aid from Arab countries hardly changed, increasing from $0.1 billion in 1970 to $0.3 billion in 1999.

25. During the 1990s aid to Africa as a portion of donors' gross national product (GNP) increased in just 4 of 21 DAC countries: Denmark, Ireland, Luxembourg and New Zealand. The OECD target for aid to all developing countries is 0.7 per cent of DAC members' GNP, but few members have achieved that goal. Still, in 1991-1999 some rich countries provided significant aid to Africa — Norway provided aid equal to 0.30 per cent of its GNP, Denmark and France provided 0.28 per cent, Sweden provided 0.22 per cent and Portugal provided 0.18 per cent. The world's two largest economies, Japan and the United States, provided Africa with aid equal to just 0.04 per cent of their GNP.

26. The DAC countries' per capita provision of aid to Africa varies considerably, from $91 per person in Denmark to $0.06 per person in New Zealand in 1999. The most generous donors in per capita terms are Denmark, Luxembourg, Norway, France and Sweden. Seen from another perspective, in 1999 France provided $3.50 in aid per African, the United States provided $2.79 and Japan provided $1.75. Except for Denmark, Ireland, Luxembourg, New Zealand and Portugal, DAC countries cut aid per African in the 1990s, with the largest declines occurring in the United States, Finland, Italy, Sweden, Canada and Germany. Of the 21 DAC countries, 16 provided less than $1 in aid to the average African in 1999, and 14 donated less than $0.50.

African economies grew faster than expected

27. In 2001 just 16 African countries experienced GDP growth of less than 3 per cent, down from 27 countries in 2000. The number of countries with growth rates exceeding 3 per cent increased from 26 in 2000 to 37 in 2001, and 3 more countries are expected to join this group in 2002. Thus, most African countries appear to be converging towards growth rates above the "traditional" 3 per cent — with positive implications for poverty reduction.

28. In recent years Africa's slower GDP growth relative to other developing regions has been attributed to its more restrictive conditions on aid, trade and foreign direct investment. Underlying these factors, however, are the inadequate production and management systems that have resulted from years of poor economic management and social and political instability. To close the performance gap,

Africa needs to upgrade its technology and, more important, develop democratic and tolerant political systems, strengthen regional and national security and foster sound economic management.

29. During 1999 and 2000 Africa's terms of trade improved considerably — mainly because of higher oil prices and a partial recovery in gold and metal prices — leading to stronger fiscal and current accounts. In addition, the region's debt burden declined as a result of higher export earnings and the provision of debt relief to some countries.

30. Africa's average per capita income grew by an estimated 1.9 per cent in 2001 — better than the 0.7 per cent increase in 2000 but still not sufficient to achieve the international development goal of cutting poverty in half by 2015. In 2001 30 African countries achieved per capita income growth above 1.5 per cent, and in 2002 this number is expected to increase to 32. Still, raising per capita income remains the biggest challenge for African Governments and their development partners.

31. Slow growth in per capita output reflects the absence of growth in productivity, which in turn is caused by poor resource management and a lack of technological progress. If Africa is to achieve the international development goals, these issues must be addressed.

Performance by subregion

32. Except for southern Africa, all African regions achieved decent economic performance in 2001, especially North Africa, where GDP growth averaged nearly 6 per cent. Southern Africa's GDP grew by just 2.4 per cent, down from 3 per cent in 2000, mainly because of negative growth in Zimbabwe and slower growth in South Africa, reflecting poor harvests. After falling in 2000, average GDP growth rose to 3.3 per cent in West Africa and 5 per cent in East Africa, driven by lower prices for oil imports and higher prices for agricultural exports. In 2002 GDP growth is expected to accelerate in East and southern Africa and slow in North and Central Africa.

33. The five largest African economies — South Africa, Algeria, Egypt, Nigeria and Morocco, which account for 59 per cent of African GDP and contain 36 per cent of the continent's population — grew by 4.3 per cent in 2001, up from 3.2 per cent in 2000 and 2.7 per cent in 1999. This better performance was due to rapid economic growth in Algeria, Egypt and Morocco. Although South Africa experienced more stable mineral prices in international commodity markets, it had the slowest growth rate in this group.

34. Africa's 11 oil-exporting countries account for half of the continent's GDP and just over a third of its population. In 2001 their GDP growth averaged 5.8 per cent, up from 4.1 per cent in 2000. Among the 42 non-oil exporters, growth averaged 3.7 per cent in 2001, up from 2.9 per cent in 2000 and 2.7 per cent in 1999. Lower oil prices explain the better performance of the non-oil economies in 2001.

Performance of agriculture and industry

35. Agriculture significantly influences the performance of most African economies. It accounts for 24 per cent of Africa's GDP, 40 per cent of its foreign exchange earnings, and 70 per cent of its employment. In 2000 about 56 per cent of

Africans (431 million people) depended on agriculture for their livelihoods. In East Africa agriculture accounted for 39 per cent of GDP, in West Africa 37 per cent, in Central Africa 21 per cent, in North Africa 17 per cent and in southern Africa 11 per cent. Although the primary functions of agriculture have to do with the production, exchange, and consumption of agricultural products, the sector has important implications not recognized in the marketplace: natural resource management, environmental preservation, social cohesion and stability, and cultural continuity and heritage. Hence, agricultural development must promote not only output growth but also improvements in natural resource management and social stability.

36. During 2000 42 African countries achieved agricultural growth. The top performers were Malawi (12.7 per cent), Seychelles (9.5 per cent), Zambia (7.4 per cent), Tunisia (6 per cent), Senegal and the Niger (5.8 per cent each), Mali (5.3 per cent) and the Sudan (5 per cent). Nine countries experienced negative growth, largely because of delays in seasonal rains: Guinea Bissau (-5.3 per cent), Djibouti (-2.7 per cent), Mauritius (-2.4 per cent), the Republic of the Congo (-2.1 per cent), the Democratic Republic of the Congo (-1.8 per cent), Côte d'Ivoire (-1 per cent), Somalia (-0.5 per cent), Equatorial Guinea (-0.4 per cent) and Togo (-0.3 per cent). Southern Africa was the best regional performer (5.2 per cent), followed by West Africa (3.5 per cent) and North Africa (3.2 per cent).

37. Despite massive efforts and investments in agriculture by African Governments and their development partners, the sector remains heavily dependent on the weather and largely traditional, dominated by an illiterate and poor workforce and overwhelmed in some countries by civil instability. Recent agricultural policies have placed too much reliance on market forces, neglecting more fundamental structural issues such as technology and extension services, marketing infrastructure and civil conflicts over land and pasture.

38. Industry in Africa continued to face challenges because of foreign competition, lack of skilled workers and limited financial resources. In 2000 the industrial sector — comprising manufacturing, mining, construction, and electricity, gas and water — accounted for 33 per cent of Africa's GDP, with manufacturing and mining accounting for three quarters of the total.

39. Many countries secured industrial growth in 2000, notably Uganda (15.2 per cent), Lesotho (11.8 per cent), Angola (7.9 per cent), Mozambique (7.8 per cent), Ethiopia (7.5 per cent), Burkina Faso (7 per cent), Benin (6.8 per cent), Algeria (5.9 per cent), Tunisia, Tanzania and Botswana (5.7 per cent each) and Senegal (5.6 per cent).

40. The fastest-expanding industrial subsector was electricity, gas, and water (with a growth rate of 4.9 per cent), followed by construction (3.9 per cent) and mining (3.5 per cent). African manufacturing grew by 2.5 per cent in 2000, led by growth in East Africa (4.4 per cent) and southern Africa (3.5 per cent).

41. Mining accounted for a substantial share of industrial growth and remains the key to industrial prosperity in many African countries, a potential that has yet to be fully exploited. Africa contains about 30 per cent of the earth's mineral reserves, including 40 per cent of gold, 60 per cent of cobalt and 90 per cent of platinum. In 2000 the best performers in mining were Ethiopia (13 per cent growth), Mozambique (10.3 per cent), Burundi (9.5 per cent), Benin (8.7 per cent), Angola (8.6 per cent), Algeria (7.5 per cent), Botswana (6.2 per cent), Ghana (5.8 per cent),

Uganda (5.6 per cent), and Togo and Senegal (5 per cent each). The worst performers were Sierra Leone (-10.3 per cent), the Democratic Republic of the Congo (-2.8 per cent) — both as a result of civil instability — Côte d'Ivoire (-1.2 per cent) and South Africa (-1 per cent).

42. From 1980 to 1999 Africa's known oil reserves grew by 1.96 per cent a year and oil production by 0.38 per cent a year. Yet because of increased production in other parts of the world, crude oil exports dropped from 5.1 million barrels a day in 1980 to 4.7 million in 1999. During the same period Africa's known natural gas reserves grew by 3.6 per cent, production by 9.8 per cent and exports by 10.9 per cent. In 1999 gas production increased by 6.2 per cent and gas exports by 6.4 per cent.

Consumption, savings and investment

43. African economies remain trapped in a vicious circle of low savings and investment. In 2000 spending on consumption absorbed 88 per cent of Africa's GDP, leaving little for savings and investment. In 32 of 37 countries for which data are available, general government consumption averaged 15 per cent of GDP. In the other 5 countries it was more than 20 per cent: Zimbabwe (23 per cent), Botswana (28 per cent), Namibia (29 per cent), Angola (32 per cent) and Eritrea (65 per cent).

44. Besides low incomes, the main obstacles to higher savings are inefficient financial intermediation and high macroeconomic volatility. To achieve sufficient growth, Africa requires investment of at least 25 per cent of GDP. But in 2000 gross domestic savings in the region averaged 12 per cent of GDP, indicating a wide gap — 13 per cent of GDP — between actual savings and the required investment. Still, 14 African countries have achieved savings rates above 15 per cent: Algeria (32 per cent), Angola (53 per cent), Cameroon (19 per cent), the Republic of the Congo (48 per cent), Côte d'Ivoire (23 per cent), Equatorial Guinea (58 per cent), Gabon (35 per cent), Guinea (15 per cent), Mauritius (23 per cent), Morocco (15 per cent), Nigeria (18 per cent), Seychelles (20 per cent), South Africa (18 per cent) and Swaziland (21 per cent).

45. Gross domestic fixed capital formation — spending on fixed assets such as buildings, vehicles, plants, machinery and the like — was just over 20 per cent of Africa's GDP in 2000, less than the 25 per cent required for industrial takeoff. With many countries privatizing State-owned enterprises, private investment accounts for a growing share of domestic investment and public investment for a shrinking share.

Inflation

46. In 2000 Africa's average inflation rate — excluding Angola and the Democratic Republic of the Congo — rose to 7.3 per cent, up slightly from 7 per cent in 1999. Inflation of more than 50 per cent in Angola (326 per cent), the Democratic Republic of the Congo (556 per cent) and Zimbabwe (56 per cent) reflected civil instability. But most countries, notably CFA franc countries, had inflation below 10 per cent — a remarkable achievement given the higher oil prices in 2000. CFA franc countries pursued tight monetary and fiscal policies consistent with those of the European Central Bank, and some recorded negative or less than 5 per cent inflation. This performance was aided by favourable weather, which supported satisfactory food supplies.

47. In South Africa high prices were partly caused by high fuel prices and by the depreciation in the rand relative to the United States dollar. Higher inflation in East Africa was driven by the 1999/2000 drought, which raised local food prices, and by rising petroleum prices. In North Africa inflation was subdued and is expected to stay that way in 2001-2002 due to lower food prices and higher oil prices.

Exchange rates

48. Several African countries saw their real effective exchange rates appreciate in 2000. Among the causes were worsening terms of trade, government commercial polices that placed a premium on imports and international movements of capital and income.

49. In addition, between 1999 and 2000, 44 African countries experienced depreciations in nominal exchange rates between their currencies and the United States dollar. This change mainly resulted from the adoption of flexible exchange rate regimes. In 23 countries the depreciation was less than 10 per cent, but in 5 countries it exceeded 50 per cent: the Democratic Republic of the Congo (1,011 per cent), Angola (201 per cent), Ghana (107 per cent), Malawi (72 per cent) and Zambia (58 per cent). These enormous depreciations were mainly caused by worsening political situations (as in the Democratic Republic of the Congo and Angola) or declining foreign exchange earnings resulting from poor commodity prices (as in Ghana and Malawi).

Balance of payments

50. Africa's export earnings rose by nearly 26 per cent in 2000, reflecting a 19 per cent increase in their unit value and a 6.14 per cent increase in their volume. Higher oil prices drove most of the increase in unit value. However, a 1.5 per cent increase in volume and a 1.7 per cent drop in unit value caused export earnings to fall by 0.2 per cent in 2001. Higher prices and volume were also responsible for a 6.7 per cent increase in import costs in 2001, with a 0.8 per cent increase in their unit value and a 4.8 per cent increase in their volume. The higher volume of imports was a welcome break because it enabled higher investment, increased capacity utilization in manufacturing industries and dampened inflationary pressures, particularly in oil-exporting countries, where demand surged with the higher incomes engendered by oil exports.

51. Higher unit values for exports and imports caused Africa's terms of trade to appreciate by 18.1 per cent in 2000, the largest increase since the mid-1980s. But in 2001 terms of trade fell by 2.1 per cent due to falling oil prices. In 2000 the favourable external environment — particularly for oil exporters — reversed the unfavourable position of Africa's trade account in 1998-1999. In 2001 the trade surplus in goods is estimated to have fallen to $15 billion, driven by movements in oil prices.

52. Because African countries are overly reliant on foreign freight, insurance and banking services to support their export-import trade, the continent's service balance remains in deficit. In 2001 this deficit is estimated to have fallen slightly, to $11.4 billion. Driven by higher export revenues in oil-exporting countries, the current account recorded a surplus in 2000, but this surplus was not maintained in 2001. Still, the current account deficit fell from 4.8 per cent of Africa's GDP in 1998 to 0.9 per cent in 2001.

Economic policies have focused on boosting growth and reducing poverty

53. Driven by a desire to rapidly reduce poverty, economic policies in Africa in 2000-2001 sought to promote macroeconomic stability and higher growth and to improve the delivery of social services (see box 2). Many Governments revived stalled structural reforms such as deregulation and external liberalization. The main themes of economic policy included creating an enabling environment for producers, investors and employers and improving governance and public finances.

54. Stabilization and structural adjustment programmes focused on maintaining tight fiscal and monetary policies and on realigning exchange rates. These measures were complemented by efforts to restructure financial markets, deepen customs and tax reforms, strengthen budget procedures and fiscal discipline, and restructure industrial relations and legal and judicial systems. Many African countries adopted the poverty reduction strategy framework introduced by the World Bank and the International Monetary Fund, which requires developing clear strategies for investing the savings from debt relief in poverty reduction programmes and defining the human, social and political environment in which poverty reduction is to be achieved.

Box 2
The New Partnership for Africa's Development — an African framework for faster growth and development

The New Partnership for Africa's Development (NEPAD) is a pledge by all of Africa's leaders to eradicate poverty and move towards sustainable growth and development. The Partnership focuses on African ownership of the development process and seeks to reinvigorate the continent in all areas of human activity. Through the Partnership, African leaders have agreed to:

- Strengthen mechanisms for conflict prevention, management and resolution;
- Promote and protect democracy and human rights by developing standards for accountability, transparency and participatory governance;
- Restore and maintain macroeconomic stability;
- Implement transparent legal and regulatory frameworks for financial markets;
- Revitalize and extend education, technical training and health-care services;
- Promote women's role in social and economic development;
- Promote the development of infrastructure, agriculture, agroprocessing and manufacturing to meet the needs of export and domestic markets and local employment.

The NEPAD document draws Africans' attention to the seriousness of the continent's economic challenges, the potential for addressing them and the challenge of mobilizing support for change. The main strategies proposed include:

- **Fostering conditions for long-term peace, security, democracy and good governance;**
- **Promoting the provision of regional and subregional public goods such as water, transportation, energy, environmental management and other infrastructure, notably telecommunications;**
- **Developing education and human resources at all levels, and in particular increasing the role of information and communication technologies in education and training;**
- **Increasing domestic resource mobilization and accelerating foreign investment;**
- **Creating a conducive environment for private sector activities, with an emphasis on domestic entrepreneurs;**
- **Promoting the inflow and effective use of official development assistance (to support the provision of international public goods in Africa) by reforming systems for delivering and evaluating aid;**
- **Pursuing gender equality in education, business and public service;**
- **Supporting efforts by the Economic Commission for Africa to strengthen Poverty Reduction Strategy Paper learning groups.**

55. Some African countries, suffering from political turmoil and in some cases armed conflict, will not reap all the expected short-term benefits of such reforms. In other countries HIV/AIDS has undermined development efforts and placed new demands on government finances. But in the medium and long term, better economic policies should lead to better economic performance.

Fiscal policy

56. In many African countries fiscal policy is now focused on minimizing domestic debt and freeing resources for private sector activity by reducing fiscal deficits and making tax administration and government spending more transparent. But because of higher social spending, among other things, overall fiscal policy was expansionary in 2000.

57. Several Governments have increased social spending. Cameroon's implementation of the programme defined in its Poverty Reduction Strategy Paper, with the accompanying $100 million a year in interim debt service relief under the Heavily Indebted Poor Countries Debt Initiative, boosted government spending on health care, primary education, HIV/AIDS prevention, basic infrastructure and rural development. In some countries, however, social spending faces considerable challenges. To reduce its fiscal deficit from 14 per cent of GDP in 1999 to 4 per cent in 2000 while protecting social programmes, Zimbabwe had to slash other public

spending. In Angola social spending did not increase because the Government failed to complete its Poverty Reduction Strategy Paper.

58. In 2000-2001 ratios of tax revenue to GDP and of direct tax revenue to total tax revenue increased, though they remain low. Grants continued to play a substantial role in sub-Saharan Africa, accounting for more than 4 per cent of GDP, compared with about 1 per cent in North Africa. To sustain needed public spending, new strategies are required to raise tax revenues — especially through reforms of direct taxation systems. Tax reforms would generate revenue and improve macroeconomic management through automatic stabilization.

59. Second-generation fiscal reforms emphasize reducing poverty, improving governance, developing basic infrastructure and delivering social services more efficiently. These reforms will be executed through public spending planning systems such as the Medium Term Expenditure Framework and the Poverty Reduction and Growth Facility.

Monetary policy

60. To lower inflation, many African Governments adopted tight monetary policies in 2000-2001. Central banks were compelled to manage broad money supplies by deepening inter-bank money markets through more regular issues of treasury bills and more effective open market operations.

61. In the West Africa CFA zone the planned second devaluation of the CFA franc did not occur because economic growth remained positive. Thus, the CFA franc remained pegged at 656 to the euro. In 2000 inflationary pressures associated with the 1999 decline in the CFA franc led the regional central bank (Banque centrale des Etats de l'Afrique del' Ouest) to tighten its policy in line with that of the European Central Bank.

62. To encourage growth, some central banks — taking advantage of lower inflation — cut their discount rates. For example, Algeria cut its discount rate from 7.05 per cent to 6 per cent. Local banks followed suit by revising their lending rates, which fluctuated between 8 and 10 per cent in 2000, down from a range of 8.5 to 10.5 per cent in 1999. Some countries, such as Nigeria, used a band system that allowed banks to apply different rates to reflect potential investment risks. Central African CFA countries continued to pursue reasonably tight fiscal policy, while their central banks re-established a measure of restraint in monetary policy. In Ghana interest rates dropped to 39 per cent in October 2001, down from 43 per cent in January 2001.

Exchange rate policy

63. Exchange rate realignment remained a key challenge, particularly in countries with flexible exchange rates and loose monetary policies. In Africa, where CFA countries have long enjoyed fixed exchange rates through an institutional arrangement with the French Government, the 1997-1998 East Asian crisis revived a long-standing debate on the merits of flexible and fixed exchange rate systems. CFA countries have preferred fixed exchange rates to promote stable prices, but other countries have relied on managed floating rates.

64. Most African Governments are resistant to devaluing or depreciating their currencies. For example, the weakening of the euro in 2000 made the euro zone

more competitive against Moroccan exports, leading Morocco's business community to demand a devaluation of the dirham. But the Government resisted this move, given its potentially adverse effects on the cost of oil imports and on other macroeconomic conditions. In contrast, Zimbabwe abandoned its fixed exchange rate in August 2000 and carried out a series of mini-devaluations, intensifying inflationary pressures. The central bank of the Democratic Republic of the Congo devalued the currency in October 2000, narrowing the gap between the official and parallel exchange rates from 395 per cent to 90 per cent. Egypt moved from a managed float to a managed peg. Ghana's currency, the cedi, depreciated relative to the United States dollar in the first half of 2001 due to deteriorating terms of trade for cocoa (the country's primary export) and declining gold prices. But since mid-2001 the cedi has stabilized against the dollar, largely as a result of fiscal prudence.

65. To improve the external competitiveness of their economies, African Governments have been paying more attention to movements in exchange rates — particularly real exchange rates — and adopting macroeconomic policies to reduce their volatility. Among the largest African economies, real exchange rates have been relatively stable in Algeria and Morocco. Nigeria has experienced considerable volatility since the late 1990s. Finally, South Africa's rand has been depreciating since mid-2001, and in 2002 the exchange rate is expected to fall below 11 rand to the dollar, creating fears of higher inflation and lower foreign investment.

The Expanded Economic Policy Stance Index of the Economic Commission for Africa

66. The Expanded Economic Policy Stance Index, introduced in last year's *Economic Report on Africa*, combines quantitative aspects of fiscal, monetary and exchange rate policies with the results of the Country Sustainability Assessment Survey, which has been completed in 23 African countries (up from 21 in 2000). The survey's qualitative assessments give the index greater breadth than would assessments based solely on quantitative data. For example, the survey takes into account judicial independence, respect for property rights, the effectiveness of regulatory institutions and policies targeted on reducing poverty among women. The survey draws on government employees and officials, members of the business community, resident employees of international organizations, resident employees of non-governmental organizations, academics and independent professionals.

67. The scores for the Expanded Economic Policy Stance Index and the corresponding country groups — good, fair and poor — were obtained by cluster analysis. The analysis shows that the good cluster consists of 10 countries, up from 7 in 2000. This year South Africa earned the top score, inching out Botswana. This ranking is commensurate with the strong economic fundamentals reflected in the recent upgrade of South African debt by Moody's. Namibia, Swaziland and Mali round out the top five. Uganda, ranked eighth last year, slipped out of the top 10 due to uncertainties surrounding the 2001 presidential election and cross-border conflicts in the Democratic Republic of the Congo and the Sudan.

68. Ethiopia moved from fair to good based on its Interim Poverty Reduction Strategy Paper, good targeting of poverty reduction efforts on the most disadvantaged, commendable HIV/AIDS awareness, low inflation and cessation of hostilities with Eritrea. The poor performers were joined by Kenya, which is

plagued by political uncertainty and weak regulatory institutions. Otherwise there were no changes at the bottom of the league, with Burundi, Liberia and the Sudan receiving the lowest scores, mostly because of civil or political conflict and economic mismanagement. The average score for the entire sample rose to 4.7, from 4.2 in 2000, suggesting general progress in improving economic policies.

The outlook for 2002 is cautiously optimistic

69. The outlook for African economies in 2002 is shaded by the global slowdown, particularly as it affects South Africa, the continent's largest economy. But South Africa's outlook for 2002 is positive, because strong economic fundamentals and a stable macroeconomic environment should allow for continued robust expansion over the medium term. Despite increased uncertainty about global economic prospects in the wake of the attacks of 11 September, international investors are not writing off emerging markets as an asset class but instead are viewing countries on their own merits.

70. South Africa's international credit rating, already in the prime investment grade category, was recently upgraded by Moody's Investors Service. The country's foreign debt is stable at about 30 per cent of GDP, and public debt has fallen to 47 per cent of GDP — well below the internationally accepted safe level of 60 per cent. In the medium term it is unclear what effect Moody's upgrade will have on foreign portfolio investment flows, but it will certainly lower the cost of government borrowing in international loan and bond markets. GDP growth is forecast to be 3.5 per cent in 2002, up from 3 per cent in 2001.

71. The three large North African economies — Egypt, Morocco and Tunisia, which account for 25 per cent of Africa's GDP — provide the greatest potential benefits for Africa in 2002. Macroeconomic conditions are favourable in all three countries: inflation is low, external reserves are adequate, debt has been reduced to more acceptable levels and substantial progress has been made on structural reforms (particularly privatization and price decontrol).

72. Although the global economic slowdown will likely affect these economies because of their deeper integration with the world economy, strong economic fundamentals should provide a comfortable cushion in the medium term. For instance, the latest IMF statement on Tunisia lavished praise on the Government's economic and development policies. The real economy grew by 4.7 per cent in 2000 and 6 per cent in 2001, inflation remained below 3 per cent, and a flexible exchange rate, prudent fiscal and monetary policies and increased opening of the economy prevented strong growth from putting excess pressure on domestic resources. Prospects for 2002 remain positive, driven by strong manufacturing growth and solid tourism performance.

73. Morocco and Tunisia have signed cooperation agreements with the European Union, and European Union negotiations with Algeria are under way. The agreements require market-oriented reforms — such as harmonizing standards, rules, and regulations — to eliminate practices that distort trade, including monopolies, government subsidies and privileges for public enterprises. Thus, the European Union agreements will provide a strong impetus for North African countries to move towards open trade policies, with substantial benefits for growth and investment.

74. North Africa's status as one of Africa's main recipients of foreign direct investment makes it vulnerable to an expected drop in investment flows — a threat already evident before the attacks of 11 September. But this effect will likely be felt with a lag, and economic expansion in Egypt, Morocco and Tunisia should hold up in 2002. Still, North African economies remain hobbled by their narrow export base. Moreover, trade between them is limited, accounting for a small fraction of each country's total trade. Individually, North African markets are small and highly protected. Trade protectionism takes many forms, including high tariffs, valuation problems, non-tariff barriers (such as standards and regulations) and physical barriers at borders. As a result, foreign direct investment (apart from that associated with privatization) remains low, given the region's considerable potential.

75. Despite a continued decline in world cotton prices, production in West Africa is set to soar in 2002, reflecting favourable climatic conditions and government policies to stabilize farmers' incomes. For the 2000/01 season, cotton output is expected to exceed 2.1 million tons, compared with the long-term average of 1.5 million tons a year. Among francophone countries the top producers are Burkina Faso, Côte d'Ivoire and Mali, which account for about two thirds of regional production. In 2002 Mali's Government expects to more than double cottonseed production, to 560,000 tons.

76. After two years of increased spending financed by higher oil revenues, Africa's oil exporters face mixed prospects in 2002. Although they are still receiving considerable revenue, large oil exporters will likely see growth somewhat dampened by lower oil prices, smaller Organization of Oil Exporting Countries (OPEC) quotas and less favourable foreign investor sentiment. Smaller oil exporters should fare better because they are not bound by OPEC quotas, and foreign investors continue to be attracted to these countries. For instance, increased output and exports are expected to sustain growth in Angola and the Sudan, and the Sudan will also benefit from increased production of refined petroleum products.

77. With oil prices likely to stay below $20 a barrel in 2002, growth in African countries is expected to average 3.4 per cent in 2002. Thanks to booming oil revenues, real GDP growth in Equatorial Guinea — Africa's fastest-growing economy — continues to be extremely high; it was about 65 per cent in 2001. Prospects for continued growth look good with the resolution of a territorial dispute between Equatorial Guinea and Nigeria. Nigeria agreed to recognize Equatorial Guinea's sovereignty over the ExxonMobil-operated Zafiro and associated oil fields. In return, Equatorial Guinea conceded a large share of France's TotalFina fields. The agreement will likely boost oil exploration and development in deep offshore waters between the Guinean island of Bioko and Nigeria's Niger Delta.

78. Performance among non-oil exporters is also expected to improve in 2002, reflecting reduced political instability and increased agricultural output. Lower oil prices and a modest recovery in the prices of some key commodities, such as cocoa and cotton, should ease import constraints for several non-oil exporters. In many countries — the Central African Republic, the Democratic Republic of the Congo, the Republic of the Congo, Côte d'Ivoire, Eritrea, Ethiopia and Guinea — moderating political instability or the cessation of violence should improve investor and consumer sentiment, and the resumption of official financial assistance to some countries will support higher public spending. Conversely, the civil unrest that may result from upcoming presidential and parliamentary elections in Kenya, Zambia

and Zimbabwe, along with the continuing land reform controversy in Zimbabwe, will likely have a destabilizing effect on travel, tourism and general economic activity in East and southern Africa in 2002.

79. In 2002 some countries — Benin, Ethiopia, Mali, the Niger, Senegal and Tanzania — will benefit from debt relief under the enhanced Highly Indebted Poor Countries Debt Initiative. Tanzania should see debt repayments slashed from $193 million in 2000 to $116 million in 2002, a savings of $77 million. Mozambique will benefit from an estimated 73 per cent reduction in its external debt stock and a halving of its external debt service obligations.